Supreme Court, U. S.
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In the Supreme Court

of the United States

OCTOBER TERM, 1975

No. 75-1549

JAMES N. SINCLAIR, et al,

Petitioners,

v.

CHARLES E. WILLIAMS,

Respondent.

JAMES N. SINCLAIR, et al,

Petitioners,

v.

DAN R. CARLSON & FRANK YAZZOLINO,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Petitioners[1] respectfully pray that this Court grant a writ of certiorari to review the Judgment of the United States Court of Appeals for the Ninth Circuit reversing, without finding an abuse of discretion and by applying new substantive rules for proof of liability under Section 10(b) of the Securities Exchange Act of 1934, judgments of the trial court de-

[1] Petitioners are the defendants named in the complaints, other than Touche Ross & Co. and Data Pacific Corporation.

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nying class action status because individual issues would predominate over common issues and dismissing plaintiff Williams' claim under SEC Rule 10b-5 because he admittedly was not influenced by the very prospectus he alleges to be misleading. Remand is appropriate to consider *Ernst & Ernst* v. *Hochfelder*, (March 20, 1976) — U.S. —.

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the Ninth Circuit (by District Judge Voorhees[2] and joined in by Judges Koelsch and Ely) is reported at — F.2d —, and appears in the Appendix hereto at pp. A-14 to A-27, together with the order amending that opinion and denying petitioners' motion for rehearing (A-28 to A-29). The opinions of the United States District Court for the District of Oregon (by Judge Solomon), not reported for publication, appear in the Appendix at A-1 to A-13.

JURISDICTION

The Judgment of the Court of Appeals was dated and entered December 15, 1975. A timely petition for rehearing and rehearing *en banc* was denied by Order filed March 29, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

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[2] Sitting by designation.

QUESTIONS PRESENTED

I. May a federal appellate court, consistent with the Enabling Act[3] and the parties' rights to due process,[4] reverse the trial court's determination that the cases should not be certified as class actions because individual questions predominated over common questions:

A. Where the trial court based its determination on a careful review of the record and the appellate court did not find that the trial court abused its discretion?

B. Where the appellate court acknowledged that the statute of limitations defense presented an individual issue for each class member, but subsumed that issue under a sweeping application of the predominance and manageability provisions of Rule 23(b)(3) which nullifies substantive requirements of Section 10(b) of the Securities Exchange Act of 1934?

II. Did plaintiff Williams' admitted lack of reliance on the April 29, 1969 prospectus preclude him from asserting claims under Rule 10b-5 based on the contention that the prospectus affirmatively misstated material facts?

III. Should the dismissal judgment of the trial court be reinstated?

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[3] 28 U.S.C. § 2072.
[4] United States Constitution, Amendment V.

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Constitutional Provisions, Statutes and Rules Involved

United States Constitution, Amendment V.

Statutes:

Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b))[5]

The Enabling Act (28 U.S.C. § 2072).

Rules:

Rule 23, Federal Rules of Civil Procedure.

Rule 10b-5, Securities and Exchange Commission (17 C.F.R. § 240, 10b-5).[5]

STATEMENT OF THE CASE

Both complaints purported to be class actions filed on behalf of shareholders of Data Pacific Corporation (Data Pacific) alleging that a company prospectus dated April 21, 1969 misstated and omitted material facts in violation of federal securities laws. The principal allegations were that the prospectus affirmatively misrepresented the existence of purchase orders and the state of development of a computer information device that Data Pacific was seeking to develop and finance through the public offering.

The District Court refused to certify either as a class action, holding that individual questions predominated over common questions.[6] It focused specifically on the threshold burden each plaintiff and class mem-

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[5] Appendix, pp. A-30 to A-31.

[6] Appendix, pp. A-1 to A-7.

ber would be required to meet in order to avoid the bar of the statute of limitations, i.e., that he did not know about and had no reason to suspect any wrongdoing, or that the defendants prevented him from investigating his claim, and found, after reviewing an extensive record made after considerable discovery by all parties, that information was available to the purchasers which would have led a reasonably prudent investor to investigate his claims. That information included statements in the prospectus that the purchase orders were subject to cancellation without penalty, the rapid drop in the price of the stock after the public offering, and statements at the annual shareholders' meeting on October 20, 1969 that many purchase orders were not "firm."

The District Court later entered summary judgment[7] against plaintiff Williams on his claims under Rule 10b-5 because he admitted in his deposition that he did not rely upon and was not influenced by the prospectus in connection with his purchase.

Certain defendants then paid into Court, solely as a compromise, the amount of plaintiffs' losses, plus interest and allowable costs, totalling approximately $2,700. After a show cause hearing, at which plaintiffs appeared and testified, the District Court entered an order[8] permitting plaintiffs to withdraw the monies and dismissing their claims. Plaintiffs appealed.

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[7] Appendix, pp. A-8 to A-10.
[8] Appendix, pp. A-11 to A-13.

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The Ninth Circuit reversed the District Court on the three matters discussed above.

On the class action question, the Ninth Circuit acknowledged that plaintiffs and class members faced the individual issue of overcoming the bar of the statute of limitations, but, without finding that the District Court abused its discretion, substituted its judgment for that of the District Court and concluded, without specifying the circumstances applicable to these cases, that common questions predominated for purposes of Rule 23(b)(3). It did so mainly in reliance on its recent decision in *Blackie* v. *Barrack*, (9 Cir. 1975) 524 F.2d 891, which held that the individual issues of "reliance and damages" did not preclude a finding of predominance of common questions in a case involving only nondisclosures.

On the question of Williams' admitted lack of reliance, the Ninth Circuit held that reliance is not an element of a purchaser's claim for alleged affirmative misstatements under § 10(b) of the 1934 Act, again relying on *Blackie*.

Based on those reversals, it reversed the dismissal of plaintiff's claims.

I. The Ninth Circuit's Decision Reversing the Trial Court's Denial of Class Action Status Was Erroneous Because There Was No Abuse of Discretion by the Trial Court and Because It Nullifies the Substantive Rights of the Parties.

A. No abuse of discretion by the trial court.

1. *Statute of limitations issues preclude the predominance of common questions.*

In determining whether the requirements of Rule 23, Fed. R. Civ. P., have been met, the trial judge has broad discretion. He is best able to assess the procedure for conducting any given litigation. On review, his decision is entitled to the greatest respect. *Price* v. *Lucky Stores, Inc.*, (9 Cir., 1974) 501 F.2d 1177.[9] *Rutledge* v. *Electric Hose & Rubber Company*, (9 Cir., 1975) 511 F.2d 668, 673.

In the cases at bar, District Judge Solomon reviewed a lengthy and complicated record and conclud-

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[9] In *Price*, the Ninth Circuit held:

"A class action determination under Fed. R. Civ. P. 23 is one of a trial court's considered discretion. As was stated in City of New York v. International Pipe & Ceramics Corp., 410 F.2d 295, 298 (2d Cir. 1969), 'the judgment of the trial court should be given the greatest respect and the broadest discretion, particularly if . . . he has canvassed the factual aspects of the litigation.' This is so because the district court is in the best position to consider the most fair and efficient procedure for conducting any given litigation. Such a determination by the court will not be disturbed on appeal unless the party challenging it can show an abuse of discretion. Wilcox v. Commerce Bank of Kansas City, 474 F.2d 336 (10th Cir. 1973); Castro v. Beecher, 459 F.2d 725 (1st Cir. 1972); Hackett v. General Host Corp., 455 F.2d 618 (3d Cir. 1972); City of New York v. International Pipe & Ceramics Corp., supra." 501 F2d at 1179.

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ed that the existence of individual issues precluded a finding under Rule 23 (b) (3) that "the questions of law or fact common to the members of the class predominate over any questions affecting only individual members."

Contrary to *Price*, the Ninth Circuit did not make a specific showing or finding that Judge Solomon's procedural ruling was not supported by substantial evidence, or was based on an erroneous legal standard and constituted an abuse of discretion. That error was compounded by substituting its judgment for that of the trial court without consideration of the practical and procedural difficulties of trying the claims as a class action, and without discussion or concern about the resulting elimination of substantive rights of the parties. It held:

> "The existence of a statute of limitations issue does not compel a finding that individual issues predominate over common ones. Given a sufficient nucleus of common questions, *the presence of the individual issue of compliance with the statute of limitations* has not prevented certification of class actions in securities cases. [citations omitted]
>
> "The record before us leads us to the conclusion that common questions predominate over individual ones in both the Williams and the Carlson/Yazzolino actions and that a class action would be a superior means for the fair and efficient adjudication of each of those controversies." (A-23; emphasis added).

It is significant that the Ninth Circuit did not disturb Judge Solomon's holdings that each plaintiff

faced a statute of limitations defense as to all of his claims, and characterized that defense as an "individual issue." Thus, it affirmed, implicitly if not explicitly, Judge Solomon's findings[10] that a thorough reading of the prospectus might have alerted an investor to the possibility of cancellation of orders, and that statements at the October 20, 1969 shareholders' meeting and the rapid drop in the price of the stock after April 1969 warranted further investigation by a reasonably prudent investor, and his holding that the statute of limitations starts running when the claimant first knew or, by reasonable investigation, could have discovered that he had a claim.[11]

Not only does the limitations defense place in jeopardy each plaintiff's right to champion his claims and the claims of other investors,[12] it necessarily jeopardizes the claims of other investors in their own right. Resolution at trial will require the testimony of each plaintiff and class member. Given more than

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[10] Judge Solomon declined to state the effect of his findings on possible liability, A-4, thereby confining his determinations to the procedural issues at hand.

[11] The reasonable investigation requirement applies both under Oregon 2-year fraud limitation statute, *Salem Sand* v. *City of Salem*, (1971) 260 Or. 630, 492 P.2d 271 and *Dilley* v. *Farmers Ins. Group*, (1968) 250 Or. 207, 441 P.2d 594, and the federal fraud tolling doctrine, *Winkelman* v. *Blyth & Co., Inc.*, (9 Cir. 1975) 518 F.2d 530, cert. den. (1975) — U.S. —; see also *Bailey* v. *Glover*, (1875) 88 U.S. 342, 350; *Holmberg* v. *Armbrecht*, (1946) 327 U.S. 392; *deHaas* v. *Empire Petroleum Company*, (10 Cir. 1970) 435 F.2d 1223, and *Hupp* v. *Gray*, (7 Cir. 1974) 500 F.2d 993, 996-997 (price decline).

[12] A person without standing cannot champion a class. *Mintz* v. *Mathers Fund, Inc.*, (7 Cir. 1972) 463 F.2d 495; *Kauffman* v. *Dreyfus Fund, Inc.* (3 Cir. 1970) 434 F.2d 727, 734, cert. den. (1971) 401 U.S. 974.

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1,000 potential members of the *Williams* class, and unspecified other claimants in the proposed *Carlson/Yazzolino* classes, the trial court correctly concluded that there was no predominate question as to this controlling issue. Nor would class treatment be the superior method of fairly and effectively adjudicating the cases, as required by Rule 23(b)(3).

The Ninth Circuit cited four cases for the proposition that statute of limitations issues do not "compel" denial of class treatment. A-23. Three of those cases, however, did not involve a discovery or due diligence statute of limitations.[13] In the fourth, which did involve such a statute, the trial court specifically refused to examine the record to determine the probable predominance of that issue,[14] as the trial court did in the cases as bar.

The Ninth Circuit principally relied upon its recent decision in *Blackie* v. *Barrack*, (9 Cir. 1975) 524 F.2d 891:

> ". . . The opinion of the court in that matter recognized that the presence of individual issues, such as *damages and reliance*, did not necessarily defeat class action consideration of alleged violation of federal securities laws." (A-22-23; fn. omitted; emphasis added).

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[13] *Umbriac* v. *American Snacks, Inc.*, (E.D. Pa. 1975) 388 F. Supp. 265, 272; *Cohen* v. *District of Columbia National Bank*, (D. D.C. 1972) 59 F.R.D. 84, 90; *Dolgow* v. *Anderson*, (E.D. N.Y. 1968) 43 F.R.D. 472.

[14] *Lamb* v. *United Security Life Co.*, (S.D. Ia. 1972) 59 F.R.D. 25, 34-37.

Blackie is inapposite.'[15] It did not involve the crucial limitations issues present in these cases. It involved review of the trial court's grant of class certification, not a trial court denial after careful review of the record. It involved open market trades to which the issuer was not a party, not purchases directly from the issuer and its underwriters. It involved "impersonal stock exchange" transactions which, in the view of the Ninth Circuit, supported the dual presumptions that an issuer's material nondisclosures inflate the market price and investors rely on the integrity of such market information in establishing the trading price—thereby establishing presumptive causation/reliance; the present cases involved a price set by the issuer and its underwriters without reference to market transactions and with an opportunity for each investor, by review of the prospectus, to determine the fairness of the price—thus permitting actual proof or disproof of causation/reliance. And *Blackie* involved charges of nondisclosure, not charges of affirmative misstatement.

2. *Other individual issues preclude the predominance of common questions.*

Reliance and Causation. The principal claims are alleged misstatements in the prospectus relating to the issuer's backlog of purchase orders, and the state of development of the issuer's principal product. To

[15] *Blackie* was decided after the present cases were argued. Petitioners' motion for reconsideration of the decision at bar, which sought the opportunity to brief and argue against *Blackie*, was denied.

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recover, a purchaser of the issuer's stock must, as a minimum, present evidence that he received, read and relied upon the alleged misstatements. *Affiliated Ute Citizens of Utah* v. *United States*, (1972) 406 U.S. 128, 152.[16]

The Ninth Circuit blindly followed *Blackie:*

> "In their briefs, appellees argue that the question of individual reliance should defeat class certification. . . . The reliance issue has been resolved by *Blackie* v. *Barrack, supra*. . . ." (A-23)

Blackie did not involve alleged misstatements, and thus is not applicable. Moreover, applying *Blackie* to eliminate reliance/causation with respect to the alleged misrepresentations in the present cases squarely conflicts with *Affiliated Ute*. See also *Blue Chip Stamps* v. *Manor Drug Stores*, (1975) 421 U.S. 723 (a § 10(b) claim must be based on a purchase "in connection with" the claimant's purchase).

Multiple defendants. Neither court below had an opportunity to assess the impact of *Ernst & Ernst* v. *Hochfelder*, (March 30, 1976) — U.S. —. That case held that proof of an intent to deceive is essential to establish a defendant's liability under § 10(b) of the Securities Exchange Act of 1934. It explicitly over-

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[16] Although *Affiliated Ute* mainly involved nondisclosures under circumstances amounting to a scheme or practice to defraud under clauses (1) and (3) of Rule 10b-5, where defendants were charged with stringent contractual and fiduciary duties with respect to helpless Indian wards, clause (2) of Rule 10b-5 was cited in the context of affirming liability where plaintiffs had shown an intentional misstatement, reliance and resulting damage. 406 U.S. at 152, affirming *Reyos* v. *United States* (10 Cir. 1970) 431 F.2d 1337 at 1347.

ruled *White* v. *Abrams*, (9 Cir. 1974) 495 F.2d 724, which had sanctioned a much less onerous "flexible duty" standard, i.e., negligence. It rejected vicarious liability based on negligent aiding and abetting. The complaints do not allege that any defendant intended to deceive plaintiffs. Moreover, there are 19 defendants in these cases, including the issuer, certain of its managing officers, its inside directors, its outside directors, its accountants, its attorney, its principal underwriters, and various broker-dealers who participated in the public sale of the stock. Plaintiff's purchases were over a four-month period, and they seek to represent subsequent purchasers. Williams filed in time to assert a claim under § 11 of the Securities Act of 1933 (also subject to the limitations defense), but Carlson and Yazzolino did not. The marshalling of evidence relating solely to liability issues will present numerous and difficult individual questions and occupy considerable court time.

Damages. In *Blackie*, the Ninth Circuit recognized that the amount of damages is "invariably an individual question," but concluded that it would be "virtually a mechanical task" and hence could not defeat class action treatment. 524 F.2d at 905. In the present cases, however, where the alleged wrong cannot be quantified by reference to a market barometer, the computation of damages cannot be said to be a mechanical task or to negate proof of each investor's particular circumstances.

Cumulative effect. The cumulative effect of all in-

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dividual issues—due diligence for the statutes of limitations, reliance and causation resulting from alleged misstatements, the liability standards for each of 19 defendants under different theories of liability, and computation of damages—reinforce the trial court's determination that common questions do not predominate.

3. *Plaintiffs unwilling to pay for notice to class members.*

The record before the trial court established the unwillingness of plaintiffs to pay the cost of sending notices to class members. After class certification had been denied, this court issued its opinion in *Eisen* v. *Carlisle & Jacquelin*, (1974) 417 U.S. 156, holding, in part, that unwillingness of a plaintiff to bear such cost is a ground for dismissal of a class action. The Ninth Circuit was urged by petitioners to consider that point, but did not discuss it in its opinion.

B. The Ninth Circuit's decision improperly nullifies the substantive rights of the parties.

The Ninth Circuit's decision erroneously holds that plaintiffs' substantive duty to prove reliance/causation under § 10(b) may be eliminated to satisfy the procedural requirements of predominance, superiority, and manageability under Rule 23. It thereby conflicts with *Affiliated Ute*, which requires plaintiffs to prove actual reliance and causation to recover for *affirmative* misstatements under Rule 10b-5(2). 406 U.S. at 152. *Affiliated Ute* does not condone presump-

tions where live testimony can supply the required substantive element.

The Ninth Circuit's decision is based mainly on *Blackie*, which in the context of reviewing a procedural ruling granting class certification, held that reliance/causation for *nondisclosures* can be presumed as to each class member by showing "materiality as to all." 524 F.2d at 907, fn. 22. Defendants may then, as a matter of defense, disprove materiality as to individuals, subject to the right of the court to make materiality "conclusive" if proof of the defense should render the case unmanageable. Id.

The resulting emasculation of substantive rights under the guise of procedural rulings is fundamental error. The objective test of materiality is substituted for subjective reliance/causation. A generalized test is substituted individual proof. No purchaser need be called to testify why he purchased. Defendants cannot cross examine on that vital issue. Rebuttal evidence showing that a purchaser had other reasons to buy loses its probative impact because its target is an abstract hypothesis, not a live witness. Rebuttal evidence on other liability issues cannot focus on particular representations, but must rebut all.

Such presumptions clearly violate the mandate of § 10(b) that the wrong be "in connection with" particular purchases. *Affiliated Ute, supra;* cf. *Blue Chip Stamps, supra.*

They also violate the Enabling Act, 28 U.S.C. § 2072, which states that the Federal Rules of Civil

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Procedure shall not ". . . abridge, enlarge or modify any substantive right. . . ." Defendants' rights to refute liability (e.g., lack of intent to deceive or reliance/causation[17] under § 10(b)) and establish defenses (e.g., the lack of reasonable diligence of each purchaser for purposes of the statute of limitations) are curtailed, thereby increasing their liability and damage exposure. The rights of plaintiffs, and the class members they purport to represent, correspondingly are enlarged. The interests of absent class members are abridged by the holding in *Blackie* (524 F.2d at 911) that the right to opt out can substitute for adequate representation by a named plaintiff who purchased or sold at a different point in time and for different reasons.

Finally, the threat of curtailing defenses to keep plaintiffs' actions from becoming unmanageable violates due process. The Fifth Amendment requires that defendants have an opportunity to present every available defense. *Lindsey* v. *Normet*, (1972) 405 U.S. 56, 66; *American Surety Co.* v. *Baldwin*, (1932) 287 U.S.

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[17] In *Blackie*, the Ninth Circuit definitely intended to construe substantive rights: "Defendants contend that elimination of individual proof of subjective reliance alters and abridges their substantive rights in violation of the Rules Enabling Act, 28 U.S.C. § 2072. The obvious answer is that the standards of proof of causation we have set out apply to all fraud on the market cases, individual as well as class actions. No interpretation of Rule 23 is involved, and the Rules Enabling Act limitation is not implicated.[24] . . . [fn.] 24. Indeed, we could, in the exercise of our Article III jurisdiction, transform the 10b-5 suit from its present private compensatory mold by predicating liability to purchasers solely on the materiality of a misrepresentation (i.e., economic damage) regardless of transactional causation, without implicating the Enabling Act limitation." 524 F.2d at 908.

156, 168. The Fifth and Fourteenth Amendments require that defendants be given a fair opportunity to rebut arbitrary and unreasonable presumptions. *Vlandis* v. *Kline*, (1973) 412 U.S. 441, 446; *Manley* v. *Georgia*, (1929) 279 U.S. 1, 6. Under *Blackie*, the trial court is given impermissible discretion to prohibit proof of such defenses and rebuttal, and defendants are deprived of the full and fair opportunity to prove such defenses and rebuttal by being forced to make choices at trial based solely on manageability.

II. The Ninth Circuit Erred by Holding That Undisputed Evidence Negating Reliance and Causation Did Not Defeat Williams' Rule 10b-5 Claim.

The trial court correctly held that undisputed evidence negating reliance defeated Williams' Rule 10b-5 claim. It found that Williams' deposition testimony established that he did not rely on the prospectus containing the alleged misstatements, and granted summary judgment dismissing his Rule 10b-5 claim. The findings, which are not disputed[18] were as follows:

> "Williams received the April, 1969, prospectus before he made his fifth purchase, but he did not recall whether he read the prospectus before he purchased the shares. He admitted that even if he

[18] The Ninth Circuit stated:

> "Although that deposition was not included in the record, it is evident from the portions quoted in the briefs of counsel and from the order granting summary judgment that Williams had received and arguably had read the 1969 prospectus prior to his purchase of shares." A-25.

All parties to the appeal *designated* that deposition as part of the record. In any event, the Ninth Circuit accepted the trial court's findings as to its contents, and declined the invitation to consider it at a rehearing.

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did read the prospectus, he did not rely on any specific representation. He purchased the stock in May, 1969, for the same reasons he purchased the stock on the four prior occasions. The only difference was that in May, 1969, he thought Data Pacific was doing him a favor by issuing warrants to existing stockholders before a general public offering."

The Ninth Circuit's reversal misapplied the undisputed facts and misconstrued the legal requirements for misstatement liability. It held:

". . . Because the purchase by Williams of additional shares followed his receipt of the prospectus, the transactional nexus between the alleged fraud and the loss, required by *Raschio* v. *Sinclair*, 486 F.2d 1029 (9th Cir. 1973), is present and, in the light of the reasoning of *Blackie* v. *Barrack*, further proof of reliance is not required. While a defendant is still free to attempt to disprove causation as to a particular plaintiff, there remain material issues of fact in connection with the Rule 10b-5 claim of Williams and that claim should not have been dismissed." (A-25-26).

The Ninth Circuit committed reversible error for the following reasons:

First, in an affirmative misrepresentation case, positive proof of reliance is required. *Affiliated Ute, supra*, 406 U.S. at 152; see also *Schlick* v. *Penn-Dixie Cement Corporation*, (2 Cir. 1974) 507 F.2d 374, 380. Unlike a case of pure nondisclosure, the plaintiff can testify about his subjective reaction to the challenged prospectus and alleged misstatements. Williams did

so in his deposition, and clearly established that he was not influenced by the contents of the prospectus. *Blackie* was a nondisclosure case, and thus inapplicable.

Second, the Ninth Circuit failed to heed the inescapable conclusion that Williams' testimony negated causation. It did so by the *Blackie* approach of elevating mere temporal sequence, i.e., Williams purchased after the prospectus was issued, to a presumption of reliance/causation, and shifting to defendants the burden to "disprove causation." The obvious conclusion from Williams' testimony is that the prospectus did not cause him any harm. The trial court's judgment is consistent with that conclusion. The Ninth Circuit's contrary holding renders meaningless the very rule it purported to follow.

Third, the Ninth Circuit's holding on the class action aspects (pp. 7-17) means that defendants now face a class action championed by a purchaser whose right to recover has been disproved by his sworn testimony, but who might prevail if the trial court determines that manageability requires that the presumption of reliance/causation should become conclusive, or, should evidence disproving causation be allowed, if the trier loses sight of Williams' testimony in weighing the testimony of 1,000 other purchasers. In this light, the statutory and constitutional proscriptions discussed above (pp. 14-17) became germane.

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III. The Ninth Circuit Erred in Reversing the Trial Court's Dismissal of These Cases After Defendants Paid Into Court the Full Amount of Plaintiff's Compensable Losses as a Compromise.

After the trial court's denial of class treatment, certain defendants, solely as a compromise, offered to pay into Court the full amount of plaintiffs' compensable losses if they should prevail at trial. The payments totalled about $2,700. After a show cause hearing, at which plaintiffs appeared and testified, the trial court ordered that plaintiffs could apply for payment of those monies and dismissed the actions.

The Ninth Circuit reversed because of its holdings discussed in I and II above. Because the latter holdings constituted reversible error, the former holding should also be reversed, and the trial court's dismissal should be reinstated.

CONCLUSION

For the reasons set forth above, petitioners respectfully pray that this Court grant a writ of certiorari to review the Judgment of the United States Court of Appeals for the Ninth Circuit. If this Court declines full review as requested above, it is urged to remand these cases to the Ninth Circuit to review them in light of *Ernst & Ernst* v. *Hochfelder*, supra.

DATED April 23, 1976.

Respectfully submitted,

Leigh D. Stephenson, Attorney for Petitioners: James N. Sinclair, Harold L. Minor, Bruce M. Hall, Millard F. Berglund, Harry S. Coleman, Frank R. Cooper, Douglas D. McIver, Donald J. Olson, J. Sheldon Jones, Jr., June S. Jones Co., Somers, Campbell, Grove, Lind & Collins, Inc., Donald C. Sloan & Co., Hughbanks Incorporated, Russell, Hoppe, Keller & Balfour, First California Company, Incorporated, Daugherty Cole, Inc., E. M. Adams & Co.

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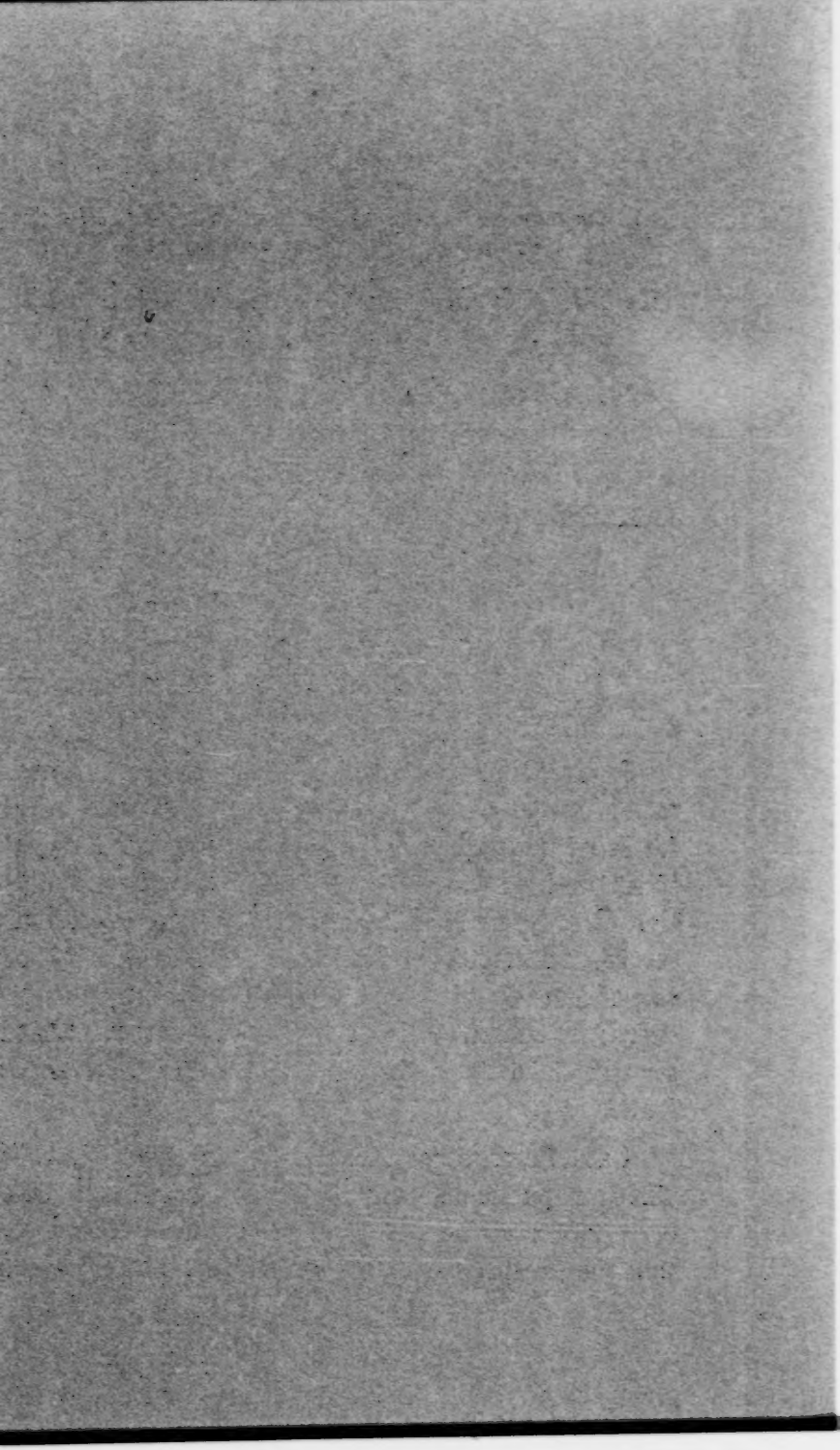

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APPENDIX

1. Opinion and Order of the District Court (Carlson) filed January 30, 1973, denying class.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

DAN R. CARLSON and FRANK YAZZOLINO,
Plaintiffs,

v.

JAMES N. SINCLAIR, et al,
Defendants.

Civil No. 72-672

OPINION AND ORDER

SOLOMON, Judge:

Plaintiffs are stockholders of Data Pacific Corporation, an Oregon corporation. They filed this action for relief under the 1933 and 1934 Securities Acts and Rule 10b-5 of the Securities and Exchange Commission. The defendants are officers of Data Pacific and several individuals and companies connected with the sale of Data Pacific stock. The case is before me on the defendant's motion for summary judgment or, in the alternative, for an order denying this case class action status.

Data Pacific was incorporated on May 22, 1967. The first public offering of its stock was held in October, 1967, and the second in 1969. Plaintiffs contend that the prospectus for the second public offering con-

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tained material omissions. They assert that because of these omissions, existing stockholders either exercised warrants or retained their shares of Data Pacific stock. Plaintiffs also contend that new and existing stockholders were fraudulently induced to buy stock in the 1969 public offering and in the aftermarket.

This is the third in a series of cases brought by various Data Pacific stockholders who charge the same securities fraud. All of them are represented by the same attorneys.

The first case, *Raschio* v. *Sinclair*, was filed in May, 1971. Raschio sought to represent all the Data Pacific shareholders. The Court denied class action status because Raschio's attorneys mailed an unauthorized solicitation to a large number of the prospective members of the class. The Court also granted the defendants' motion for summary judgment on Raschio's individual claim.

Williams v. *Sinclair* was filed in August, 1971. This was immediately after class action status was denied in *Raschio*. Williams also sought to represent all the Data Pacific stockholders. The Court permitted Williams to proceed as a representative of:

1. all those who owned Data Pacific stock on the date of the April, 1969, prospectus and who retained the stock or sold the stock before August 23, 1971, and;

2. all those who owned stock as of March 17, 1969, and who, before May 1, 1969, exer-

cised warrants issued to existing stockholders.

Carlson and Yazzolino v. *Sinclair* was filed one year later. The named plaintiffs claim to represent all those who purchased Data Pacific stock in the 1969 public distribution and in the aftermarket. They seek to fill the void created by the limited class designation in *Williams*.

The second prospectus was dated April 21, 1969. Carlson purchased the shares in question in September, 1969, and Yazzolino purchased his shares in May, 1969. Plaintiffs contend that this prospectus "failed to disclose" that one million dollars in purchase orders described in the prospectus were "fictitious, non-existent or forged." Plaintiffs assert that this "non-disclosure" violates 15 U.S.C. §§ 77k, 77q and Rule 10b-5.

Section 77k claims must be filed within one year of the date of discovery. 15 U.S.C. § 77m. Section 77m also states that no action under § 77k shall be brought "more than three years after the security was bona fide offered to the public." The second public offering by Data Pacific was held in April, 1969. The present action was filed in August, 1972. Therefore all claims arising under § 77k are barred by the statute of limitations.

Both Rule 10b-5 and § 77q do not provide for a period of limitations. Absent a federal statute of limitations, state statutes of limitations will be applied. *Sackett* v. *Beaman*, 399 F.2d 884 (9th Cir. 1968). In this district, Rule 10b-5 actions must be brought with-

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in two years of the date of actual discovery of the fraud or the date on which reasonable investigation would have revealed a claim. *Hoffert et al* v. *E. F. Hinkle & Co., Inc.*, 56 F.R.D. 395 (D. Or. 1972). Because the language of § 77q is almost identical to that of Rule 10b-5, I conclude that the reasoning and holding of *Hoffert, supra*, applies to actions brought under § 77q.

The prospectus disclosed that the purchase orders were subject to cancellation and that the company would not assert any penalty for cancellation. I do not, at this time, express any opinion on the effect of this disclosure on possible 10b-5 or § 77q liability. Nevertheless, I believe that a thorough reading of the prospectus might have alerted an investor to the possibility of cancellation.

The annual meeting of Data Pacific was held on October 20, 1969. The minutes of this meeting show that the president of the corporation admitted that many of the purchase orders were not "firm." The price of Data Pacific stock dropped rapidly after the second public offering in April, 1969. I find that by the end of 1969 there was sufficient information available to the public to warrant an investigation by a reasonably prudent investor.

Plaintiffs contend that by the filing of the two previous class actions, the statute of limitations here was tolled. They cite *Esplin* v. *Hirschi*, 402 F.2d 94 (10th Cir. 1968). In *Esplin* the Court of Appeals reversed a district court's denial of class action status.

The Court there held the statute of limitations for the class was tolled from the date of the filing of the original action in the district court. *Esplin* did not hold that the statute of limitations is tolled for prospective plaintiffs who were excluded from the original class. Under the circumstances of this case, the filing of the *Raschio* and *Williams* cases did not toll the statute of limitations in the present action.

To maintain a class action, the court must determine that "the questions of law or fact common to the members of the class predominate over any questions affecting only individual members." Fed. R. Civ. P. 23(b)3. All of the claims under Rule 10b-5 and § 77q are time barred unless a plaintiff can show that he had no reason to suspect any wrongdoing or that the defendants prevented him from investigating his claim. This presents individual questions of fact which are inappropriate for class action determination. *Hoffert, supra.*

The motion to deny class action status in the present action is granted.

The motion for summary judgment against Carlson and Yazzolino is denied except for their claims arising under 15 U.S.C. § 77k.

Dated this 30th day of January, 1973.

/s/ *Gus J. Solomon*
United States District Judge

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2. Opinion of the District Court (Williams) filed January 30, 1973, denying class.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

CHARLES E. WILLIAMS,

Plaintiff,

v.

JAMES N. SINCLAIR, et al,

Defendants.

Civil No. 71-577

OPINION

SOLOMON, Judge:

Here, as in *Carlson* v. *Sinclair*, Civil No. 72-672 (D. Or.), the plaintiff filed a class action for relief under the 1933 and 1934 Securities Act and Rule 10b-5 of the Securities and Exchange Commission. The case is before me on defendants' motion for summary judgment.

After this case was filed in August, 1971, the Court permitted Williams to represent:

1. all Data Pacific stockholders who owned Data Pacific stock on the date of the April, 1969, prospectus and who retained the stock or sold the stock before August 23, 1971; and,
2. all Data Pacific stockholders who owned stock as of March 17, 1969, and who, before

May 1, 1969, exercised warrants issued to existing stockholders.

Williams v. *Sinclair* was filed in August, 1971. The same problems on the statute of limitations for the Rule 10b-5 and 15 U.S.C. § 77q claims present in *Carlson* v. *Sinclair* are present here. I granted defendants' motion to deny class action status in *Carlson* because it appeared to me that individual questions of fact predominated over common questions. For the same reason, I hold that this action cannot proceed as a class action. Fed. R. Civ. P. 23(c)1.

There is another reason for re-examining the class designation. Williams was permitted to represent Data Pacific stockholders who retained their shares in reliance on the second prospectus. On June 28, 1972, the Court of Appeals for the Ninth Circuit decided *Mount Clemens Industries, Inc., et al* v. *Bell*, No. 71-1318, and held that to state a claim under Rule 10b-5 the plaintiff must be a purchaser or seller of the security. A large number of the stockholders represented by Williams therefore lack standing to sue under Rule 10b-5.

Dated this 30th day of January, 1973.

/s/ *Gus J. Solomon*
United States District Judge

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3. Opinion and Order of the District Court (Williams) filed February 21, 1973, granting summary judgment against plaintiff.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

CHARLES E. WILLIAMS,

Plaintiff,

v.

JAMES N. SINCLAIR, et al,

Defendants.

Civil No. 71-577

OPINION AND ORDER

SOLOMON, Judge:

On January 30, 1973, I held that this case could not be continued as a class action because individual questions predominated over common questions. I now grant defendants' motion for summary judgment on Williams' Rule 10b-5 claim, but deny summary judgment on his § 11 (15 U.S.C. § 77k) claim.

Williams contends that the April, 1969, prospectus of Data Pacific Corporation "failed to disclose" that one million dollars in purchase orders described in the prospectus were "fictitious, non-existent or forged." Williams purchased Data Pacific stock on five separate occasions. He made his first four purchases before the 1969 prospectus was issued, and these purchases are not involved in this litigation. Williams made his fifth purchase of Data Pacific stock on May

14, 1969. This purchase was through warrants issued to existing stockholders before a general public offering.

Williams received the April, 1969, prospectus before he made his fifth purchase, but he did not recall whether he read the prospectus before he purchased the shares. He admitted that even if he did read the prospectus, he did not rely on any specific representation. He purchased the stock in May, 1969, for the same reasons he purchased the stock on the four prior occasions. The only difference was that in May, 1969, he thought Data Pacific was doing him a favor by issuing warrants to existing stockholders before a general public offering.

Reliance is a necesasry element for a Rule 10b-5 recovery. *List* v. *Fashion Park, Inc.*, 340 F.2d 457 (2d Cir. 1965), *cert. denied sub. nom., List* v. *Lerner*, 382 U.S. 811 (1965). Williams did not rely on any material representation in the prospectus before he made his final purchase of Data Pacific stock. Wililams' long history of previous transactions in Data Pacific also supports this conclusion. *Colonial Realty Corp.* v. *Brunswick Corp., et al.*, 337 F. Supp. 546 (S.D. N.Y. 1971).

Williams contends that in *Affiliated Ute Citizens of Utah* v. *United States, et al*, 406 U.S. 128 (1972), the Supreme Court held that reliance is not necessary in a Rule 10b-5 cause of action. I disagree. *Ute Citizens* dealt with a failure to disclose market-making status. Such a non-disclosure has traditionally resulted

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in Rule 10b-5 liability because the seller has a right to know that his fiduciary is in a position to gain financially from transactions in the stock. *Chasins* v. *Smith Barney & Co.*, 438 F.2d 1167 (2d Cir. 1970). Thus, in in *Ute Citizens*, the Supreme Court concluded that "[u]nder the circumstances of this case" positive proof of reliance is not required. 406 U.S. at 153.

Here there was no evidence that Williams relied on any material representations in the prospectus. The defendants' motion for summary judgment on the Rule 10b-5 claim is granted.

Williams also seeks relief under Section 11 of the Securities and Exchange Act of 1933. Reliance is not an element in a Section 11 cause of action. *Ellis* v. *Carter*, 291 F.2d 270 (9th Cir. 1961). The defendants' motion for summary judgment on Williams' Section 11 claim is denied.

Dated this 21st day of February, 1973.

/s/ *Gus J. Solomon*
United States District Judge

4. Opinion of the District Court filed September 25, 1973, dismissing Williams and Carlson/Yazzolino.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

CHARLES E. WILLIAMS,

Plaintiff,

v.

JAMES N. SINCLAIR, et al,

Defendants.

Civil No. 71-577

DAN R. CARLSON and FRANK YAZZOLINO,

Plaintiffs,

v.

JAMES N. SINCLAIR, et al,

Defendants.

Civil No. 72-672

ORDER OF DISMISSAL

The court finds:

1. On June 25, 1973, counsel for certain of defendants, informed this court at a pretrial conference that defendants, although denying any liability but for purposes of compromise in view of the cost of litigation relevant to this controversy, were prepared to pay the full amount of each plaintiff's pending claim in compromise, settlement and disposition of these cases.

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2. On July 6, 1973, this court ordered that, if defendants deposited into the registry of this court the full amount of each plaintiff's pending claim, together with accrued interest, an order should be entered directing plaintiffs and their counsel to show cause why these cases should not be dismissed.

3. Such moneys were deposited into the registry of this court.

4. On August 29, 1973, this court entered its Order to Show Cause, a copy of which was served upon each plaintiff and their counsel, fixing September 10, 1973, as the date for hearing thereon.

5. On September 10, 1973, a hearing was held before this court at which each plaintiff and their counsel, as well as all defendants' counsel, were in attendance. At such hearing, plaintiffs failed to show cause why these cases should not be dismissed.

Based upon the above, IT IS ORDERED

1. The above-entitled cases are dismissed with prejudice.

2. Upon request by any of the named plaintiffs, the clerk of this court is directed to pay to each such plaintiff, out of the moneys heretofore deposited into the registry of this court, as follows:

To plaintiff Williams	$1,501.33
To plaintiff Carlson	1,173.32
To plaintiff Yazzolino	705.59

Such payment shall constitute payment in full and release of such plaintiff's individual claim against defendant; provided that the payment of such sum to plaintiff Williams shall not constitute payment in full and release of those claims of plaintiff Williams determined by summary judgment entered herein by the court on February 21, 1973.

DATED this 25th day of September, 1973

/s/ *Gus J. Solomon*
Judge

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5. Opinion of the Ninth Circuit filed December 15, 1975.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 73-3166

CHARLES E. WILLIAMS,
Plaintiff-Appellant,

v.

JAMES N. SINCLAIR, et al,
Defendants-Appellees.

No. 73-3169

DAN R. CARLSON and FRANK YAZZOLINO,
Plaintiffs-Appellants,

v.

JAMES N. SINCLAIR, et al,
Defendants-Appellees.

OPINION

[December 15, 1975]

Appeal from the United States District Court
for the District of Oregon

Before: KOELSCH and ELY, Circuit Judges
and VOORHEES,* District Judge

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* Honorable Donald S. Voorhees, United States District Judge, Western District of Washington, sitting by designation.

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VOORHEES, District Judge:

Plaintiffs appeal from the dismissal with prejudice of their securities fraud actions. For the reasons stated below, we reverse and remand.

Data Pacific Corporation (Data Pacific) was incorporated in 1967 under Oregon law in order that it might enter the burgeoning field of data processing. Its stock was first offered and sold to the public in 1967.

Data Pacific made a second public offering of 467,631 of its shares in the spring of 1969. As an integral part of that offering Data Pacific issued a prospectus, which became effective on April 21, 1969. The prospectus included detailed financial statements and representations as to the status of the research and development projects of the corporation. In addition, the prospectus stated that Data Pacific had orders, approximating one million dollars, for a data collection machine identified as the DP-1000. All of the offered shares were purchased by the public.

By the terms of the public offer current shareholders were given the opportunity, through warrants, to purchase additional shares at a price of $5.00 per share. The balance of the shares were offered to the general public at a price of $5.60 per share. The offering was registered by Data Pacific with the Securities and Exchange Commission.

Appellant Williams, who was a prior shareholder, purchased 238 of the offered shares. Appellants Carl-

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son and Yazzolino, who had not previously been shareholders, purchased a total of 500 shares.

In the months following the second public offering, Data Pacific experienced a series of setbacks, and its stock steadily declined in price. At the annual meeting of the corporation on October 20, 1969, its president conceded that many of the DP-1000 purchase orders, referred to in the April prospectus, were not firm. The DP-1000 never went into production, and none of the purchase orders for that machine were ever filled.

On August 19, 1971, Williams filed a complaint on behalf of a class comprised of all owners of Data Pacific stock. He named as defendants the corporation, its officers and directors, certain underwriters and an accounting firm. The complaint alleged violations of the Securities Act of 1933 and the Securities Exchange Act of 1934. Specifically, it charged violations of 15 U.S.C. § 77k, 77q and 78j as well as violations of Rule 10b-5 of the Securities and Exchange Commission (17 C.F.R. § 240.10(b)-5). It alleged that in the 1969 prospectus there were numerous non-disclosures of material facts, the principal ones being (1) that the purchase orders for the DP-1000 were, at best, contingent and, at worst, non-existent, and (2) that the DP-1000 was incomplete and unready for production and sale.

After a hearing on April 12, 1972, of the motion by Williams for certification of the class action, the court certified a class consisting of two sub-groups: (1) those persons who owned stock in Data Pacific as of March 17, 1969 and who, on or before May 1, 1969,

exercised warrants to purchase additional shares; and (2) those persons who owned Data Pacific stock at the time the 1969 prospectus was released and who either retained those shares until August 19, 1971 or who sold them at a loss between May 1, 1969 and August 19, 1971. The class did not include those persons who had purchased Data Pacific shares for the first time subsequent to the issuance of the 1969 prospectus.

Thereafter, on August 17, 1972, Carlson and Yazzolino filed a complaint, containing essentially the same allegations as the Williams' complaint, on behalf of a class consisting of those persons who had first purchased Data Pacific shares subsequent to the issuance of the 1969 prospectus.

Carlson and Yazzolino moved to have the class certified, and that motion was heard by a different court than the one which had heard and ruled upon the certification motion in the Williams' action. On January 30, 1973, the court entered an order denying to Carlson and Yazzolino the right to prosecute their action as a class action.[1] That ruling was based upon the court's determination that individual questions of fact predominated over common questions by reason of the existence of a statute of limitations defense to the Rule 10b-5 claims. In reaching this result, the Court concluded that the Oregon general fraud statute, ORS

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[1] In addition to ruling upon the class designation issue, the district judge determined that these plaintiffs' claims based upon 15 U.S.C. § 77k were barred by the applicable statute of limitations contained in 15 U.S.C. § 77m. This ruling is not challenged on appeal.

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12.110(1) eestablished the appropriate limitation period for Rule 10b-5 claims.[2]

ORS 12.110 establishes a basic two year limitation subject to the proviso that "the limitation shall be deemed to commence only from the discovery of the fraud or deceit." The court concluded that because of the disclosures at the annual meeting of Data Pacific on October 20, 1969, sufficient information had been made available to the general public by the end of 1969 to warrant investigation by a reasonably prudent investor. Accordingly, the court concluded, the claim of each plaintiff and each potential class member in the Carlson-Yazzolino action was subject to dismissal unless the claimant could show that he had no reason to suspect wrongdoing or that he was prevented by the defendants from investigating.

The court then reexamined the order which had designated the Williams case as a class action and concluded (1) that there was in that action the same predominance of individual over common questions of fact and (2) that those members of the Williams class who had not purchased additional shares but who had simply held onto their previously-purchased shares in

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[2] ORS 12.110 provides as follows:
"Within two years; determination of period in action for fraud or deceit; injuries to person from professional malpractice. (1) An action for assault, battery, false imprisonment, for criminal conversation, or for any injury to the person or rights of another, not arising on contract, and not especially enumerated in this chapter, shall be commenced within two years; provided, that in an action at law based upon fraud or deceit, the limitation shall be deemed to commence only from the discovery of the fraud or deceit."

reliance on the prospectus lacked standing to sue by reason of the purchaser-seller rule.[3] The court thereupon entered an order revoking the class designation in the Williams' action. No notice of this order was sent to those persons who had previously elected to become members of the class.

Following the entry of these orders, the defendants moved for summary judgment of dismissal against the § 11 (15 U.S.C. § 77k) and Rule 10b-5 claims of Williams. The court denied the motion for summary judgment as to the § 11 claim but granted that motion as to the Rule 10b-5 claim on the ground that there was no evidence that Williams had relied on any material representation in the 1969 prospectus.

Following this ruling, all defendants offered to settle the remaining claims of Williams, Carlson and Yazzolino. Thereafter the court entered an order that if defendants paid into the registry of the court a sum totalling the face amount of the claims of these three claimants, together with interest from date of purchase, the court would enter an order directing plaintiffs to show cause why that sum should not be paid out to them and the actions dismissed. Defendants de-

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[3] The purchaser-seller rule was first enunciated in *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2nd Cir. 1952), cert. denied, 343 U.S. 956, 72 S. Ct. 1051, 96 L. Ed. 2d 1356 (1952), where the court concluded that only actual purchasers or sellers of securities could sue for relief under Rule 10b-5. This Circuit recognized that rule in *Mount Clemens Industries, Inc.* v. *Bell*, 464 F.2d 339 (9th Cir. 1972), and the United States Supreme Court has recently noted its approval of the rule in *Blue Chip Stamps* v. *Manor Drug Stores*, — U.S. —, 95 S. Ct. 1917, 44 L. Ed. 2d 539 (1975).

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posited the required sum into the registry of the court, and the order to show cause issued.

At the show cause hearing plaintiffs expressed an unwillingness to accept the disposition suggested by the court as they wished to preserve their right to appeal from the class action rulings. The court, however, ruled that plaintiffs had failed to show cause why the actions should not be dismissed, and thereafter entered an order directing that the monies deposited in the registry of the court be paid over to plaintiffs and dismissing with prejudice both the Williams and the Carlson/Yazzolino actions.

Plaintiffs appeal from the orders striking the class action allegations in both cases, from the order dismissing plaintiff Williams' Rule 10b-5 claim, and from the order of dismissal of both actions. Williams also appeals from the failure of the court to make findings of fact pursuant to F.R.C.P. 56(d), following its denial of his motion for summary judgment.

CLASS ACTION DETERMINATIONS

A. Applicable statute of limitations:

Since there is no applicable federal statute of limitations as to Rule 10b-5 claims, Oregon law is here controlling as to those claims. Appellants contend that the appropriate statute of limitations for Rule 10b-5 actions brought in Oregon is the six year period pro-

vided for in ORS 12.080.[4] Appellees argue that the trial court correctly applied the two year limitation period found in ORS 12.100, the general fraud statute of Oregon. If appellants' contention were correct, no limitations problem would arise as both lawsuits were filed within six years after April, 1969.

This court had occasion to consider this issue in the context of Washington law in *Fratt* v. *Robinson*, 203 F.2d 627 (9th Cir. 1953). In that case the Washington general fraud statute was held to be the appropriate limitations statute. This decision was reaffirmed in *Douglass* v. *Glenn E. Hinton Investments, Inc.*, 440 F.2d 912 (9th Cir. 1971).

The trial court correctly applied the Oregon general fraud statute as the statute of limitations applicable to Rule 10b-5 actions.[5]

B. Whether common or individual questions predominate:

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[4] ORS 12.080 Within six years. (1) An action upon a contract or liability, express or implied, excepting those mentioned in ORS 12.070 and 12.110 and except as otherwise provided in ORS 72.7250;

(2) An action upon a liability created by statute, other than a penalty or forfeiture, excepting those mentioned in ORS 12.110;

(3) An action for waste or trespass upon or for interference with or injury to any interest of another in real property, excepting those mentioned in ORS 12.050, 12.060, 12.135 and 273.241; or

(4) An action for taking, detaining or injuring personal property including an action for the specific recovery thereof; shall be commenced within six years.

[5] We note that, at least since 1972, district courts in the District of Oregon have recognized ORS 12.110 to be the governing statute of limitations in Rule 10b-5 actions. See *Hoffert* v. *E. F. Hinkle & Company, Inc.*, 56 F.R.D. 395, 400 (D. Or. 1972).

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As outlined, above, the trial court grounded its class action rulings upon its finding that the existence of a statute of limitations defense made necessary separate determinations of the date when each plaintiff discovered or in the exercise of reasonable diligence should have discovered the alleged fraud.[6]

This court has very recently reconsidered the role of class actions in the enforcement of federal securities laws. *Blackie* v. *Barrack*, — F.2d — (9th Cir., Sept. 25, 1975). The opinion of the court in that matter recognized that the presence of individual issues, such as damages or reliance, did not necessarily defeat

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[6] Rule 23(a) of the Federal Rules of Civil Procedure provides as follows:

> Prerequisites to a Class Action. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.
>
> Rule 23(b)(3), under which these classes are sought to be certified, requires the trial court to find, in addition to the requisites set out in Rule 23(a), that "the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. . . ."

This circuit considered some of the problems with respect to class actions in securities cases in *Harris* v. *Palm Springs Alpine Estates, Inc.*, 329 F.2d 909 (9th Cir. 1964), and the conclusions contained therein remain largely unaffected by the amendments to Rule 23 in 1966. For an extended discussion of the amended Rule see *LaMar* v. *H & B Novelty & Loan Company*, 489 F.2d 461 (9th Cir. 1973).

class action consideration of alleged violations of federal securities laws.[7]

The existence of a statute of limitations issue does not compel a finding that individual issues predominate over common ones. Given a sufficient nucleus of common questions, the presence of the individual issue of compliance with the statute of limitations has not prevented certification of class actions in securities cases. *Umbriac* v. *American Snacks, Inc.*, 388 F. Supp. 265, 272 (E.D. Pa. 1975); *Cohen* v. *District of Columbia National Bank*, 59 F.R.D. 84, 90 (D.D.C. 1972); *Lamb* v. *United Security Life Co.*, 59 F.R.D. 25, 34-37 (S.D. Iowa 1972); *Dolgow* v. *Anderson*, 43 F.R.D. 472 (E.D.N.Y. 1968).

The record before us leads us to the conclusion that common questions predominate over individual ones in both the Williams and the Carlson/Yazzolino actions and that a class action would be a superior means for the fair and efficient adjudication of each of those controversies.

In their briefs appellees argue that the question of individual reliance should defeat class certification. In addition, they challenge the fitness of appellants to be representatives of the class. The reliance issue has been resolved by *Blackie* v. *Barrack*, *supra*. As for the

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[7] Courts in other jurisdictions have consistently reached the same conclusion. *Green* v. *Wolf Corporation*, 406 F.2d 291 (2nd Cir. 1968); *Werfel* v. *Kramarsky*, 61 F.R.D. 674 (S.D.N.Y. 1974); *Feder* v. *Harrington*, 52 F.R.D. 178 (S.D. N.Y. 1970); *Dolgow* v *Anderson*, 43 F.R.D. 472 (E.D.N.Y. 1968); *Kronenberg* v. *Hotel Governor Clinton, Inc.*, 41 F.R.D. 42 (S.D.N.Y. 1966).

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fitness of appellants to represent the class, the trial judge did not appear to regard them as unsuitable champions. We see no reason to disagree with his conclusions in that regard.

C. Purchaser-Seller Rule:

Included in the class designated by the original order in the Williams' action were those individuals who held Data Pacific shares prior to the issuance of the 1969 prospectus and who retained those shares after the issuance of that prospectus without making any further purchases or sales. In the subsequent order, revoking the class designation, the district court ruled that those individuals lacked standing to sue under Rule 10b-5 inasmuch as they neither purchased nor sold shares in reliance upon the alleged misrepresentation or concealments.

In light of the decision of the Supreme Court in *Blue Chip Stamps* v. *Manor Drug Stores*, — U.S. —, 95 S. Ct. 1917, 44 L. Ed. 2d 539 (1975), we affirm the correctness of the ruling below. The warrants offered to the existing stockholders of Data Pacific in the prospectus were neither contracts to purchase nor to sell securities within the definition of 15 U.S.C. § 78c(a).[8] The pre-prospectus shareholders, who did no more

[8] 15 U.S.C. § 78c(a)(13) provides that "The terms 'buy' and 'purchase' each include any contract to buy, purchase, or otherwise acquire."

15 U.S.C. § 78c(a)(14) provides that "The terms 'sale' and 'sell' each include any contract to sell or otherwise dispose of." See the discussion of these definitions in *Blue Chip Stamps* v. *Manor Drug Stores, supra*, n. 13, — U.S. at —, 95 S. Ct. at 1932, 44 L. Ed. 2d at 558.

than retain their shares, are hence barred by the purchaser-seller rule from maintaining an action under Rule 10b-5.[9]

DISMISSAL OF WILLIAMS' RULE 10b-5 CLAIM

The district court dismissed the Rule 10b-5 claim of Williams on the ground that affirmative proof of reliance was a necessary element of plaintiffs' case.

The opinion in *Blackie* v. *Barrack*, *supra*, includes a comprehensive discussion of the role of reliance in Rule 10b-5 cases where the claimant alleges omissions and non-disclosures. In line with *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 92 S. Ct. 1456, 31 L. Ed. 2d 741 (1972) this court held in *Blackie* that subjective reliance was not a distinct element of proof in Rule 10b-5 claims where the action was grounded upon non-disclosures rather than upon misrepresentations of fact.

The court below dismissed the Rule 10b-5 claim of Williams largely on the basis of certain statements made by Williams in a deposition. Although that deposition was not included in the record on appeal, it is evident from the portions quoted in the briefs of counsel and from the order granting summary judgment that Williams had received and arguably had read the 1969 prospectus prior to his purchase of shares. Because the purchase by Williams of additional shares followed his receipt of the prospectus, the transactional

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[9] It is clear that the § 11 claims are also barred as that statute covers only persons acquiring securities pursuant to the allegedly false registration statement. 15 U.S.C. § 77k(a).

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nexus between the alleged fraud and the loss, required by *Raschio* v. *Sinclair*, 486 F.2d 1029 (9th Cir. 1973),[10] is present and, in the light of the reasoning of *Blackie* v. *Barrack*, further proof of reliance is not required. While a defendant is still free to attempt to disprove causation as to a particular plaintiff, there remain material issues of fact in connection with the Rule 10b-5 claim of Williams and that claim should not have been dismissed.

DISMISSAL OF THE ACTIONS

By reason of our holdings with respect to the class action issue and the Rule 10b-5 claim of Williams, we are constrained to reverse the trial court's order dismissing with prejudice the actions of appellants after they had refused to accept the settlements proffered by defendants.

PLAINTIFF'S REQUEST FOR FINDINGS OF FACT

Williams assigns error by reason of the trial court's failure to make findings of fact pursuant to F.R.C.P. 56(d), following its denial of plaintiff's motion for partial summary judgment on liability.

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[10] *Raschio* v. *Sinclair* also arose out of Data Pacific's 1969 securities offering. The plaintiffs in that case had, however, purchased their Data Pacific stock prior to the issuance by the company of its allegedly fraudulent prospectus. The trial court granted summary judgment for the defendants upon the ground that plaintiffs' purchase of stock was not made in connection with the allegedly fraudulent acts of defendants. This court affirmed that summary judgment.

Plaintiff did not formally move for such findings until eight months after his motion for summary judgment was denied in all respects. He then sought some 158 separate findings of fact. By this time the pretrial proceedings had reached the stage of drafting a pretrial order incorporating a statement of agreed facts. The district court properly viewed the belated motion for findings of fact as being without merit.

For the reasons stated above the judgments of dismissal entered below are reversed and this matter is remanded for action not inconsistent with this opinion.

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6. Order of the Ninth Circuit filed March 29, 1976.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 73-3166

ORDER

On Petition for Rehearing

CHARLES E. WILLIAMS,
Appellant,

v.

JAMES N. SINCLAIR, et al,
Appellees.

No. 73-3169

DAN R. CARLSON and FRANK YAZZOLINO,
Appellants,

v.

JAMES N. SINCLAIR, et al,
Appellees.

Before: KOELSCH and ELY, Circuit Judges, and VOORHEES, District Judge.*

The court's opinion in the subject case is amended as follows:

The last incomplete paragraph, beginning with

* Honorable Donald S. Voorhees, United States District Judge, District of Washington, sitting by designation.

"Following this ruling," on page 4 of the opinion in its slip sheet form is amended to read:

> Following this ruling, all defendants except Touche Ross and Co., offered to settle the remaining claims of Williams, Carlson and Yazzolino. Thereafter the court entered an order that if those defendants paid into the registry of the court a sum totalling the face amount of the claims of these three claimants together with interest from date of purchase, the court would enter an order directing plaintiffs to show cause why that sum should not be paid out to them and the actions dismissed. Those defendants did deposit the required sum into the registry of the court, and the order to show cause issued.

The panel (Koelsch, Ely, and Voorhees) has unanimously voted to deny the Petition for Rehearing. Judges Koelsch and Ely have voted to reject the suggestion for en banc rehearing and Judge Voorhees has recomemnded that the suggestion be rejected.

The full court has been advised of the suggestion for en banc rehearing, and of the amendment to the opinion, hereinabove specified. No judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35(b).

The Petition for Rehearing is denied, and the suggestion for en banc rehearing is rejected.

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7. Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)).

REGULATION OF THE USE OF MANIPULATIVE AND DECEPTIVE DEVICES

Section 10. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

* * * * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

8. Rule 10b-5 of the Securities and Exchange Commission (17 C.F.R. 240.10b-5).

RULE 10b-5. EMPLOYMENT OF MANIPULATIVE AND DECEPTIVE DEVICES

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

FILED
MAY 25 1976

In the Supreme Court
of the United States

No. 75-1549

JAMES N. SINCLAIR, et al,
Petitioners,

v.

CHARLES E. WILLIAMS,
Respondent.

JAMES N. SINCLAIR, et al,
Petitioners,

v.

DAN R. CARLSON & FRANK YAZZOLINO,
Respondents.

BRIEF OF RESPONDENTS OPPOSING PETITION FOR WRIT OF CERTIORARI

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1. Judge Goodwin's Order Designating Class Action, filed April 12, 1972 ..... A-1

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In the Supreme Court
of the United States

No.....

JAMES N. SINCLAIR, et al,
Petitioners,

v.

CHARLES E. WILLIAMS,
Respondent.

JAMES N. SINCLAIR, et al,
Petitioners,

v.

DAN R. CARLSON & FRANK YAZZOLINO,
Respondents.

BRIEF OF RESPONDENTS OPPOSING PETITION FOR WRIT OF CERTIORARI

Petitioners' "Statement of the Case" is grossly misleading and in part incorrect.

The statement is incorrect, when it asserts that the District Court refused to certify a class. The District Court granted class designation in the Williams case on April 12, 1972, acting through the Honorable Alfred T. Goodwin, Circuit Court Judge, sitting as a District Court Judge by designation.

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This case commenced when Williams filed his class action complaint on August 19, 1971, and shortly thereafter asked for a Rule 23 class action designation. Judge Goodwin handled the case during the first nine months after it was filed, the period of greatest activity. During this time, numerous motions were filed, testing the law of the case. It was during this period that Judge Goodwin, in a carefully considered order, granted Williams two sub-classes, on April 12, 1972.[1] A few days later, on May 1, 1972, he denied a defendant's motion to reconsider his order.

Judge Goodwin, in his order, outlined his findings for class representation. Some 2,700 people were mailed notification of their class membership, at plaintiff's expense.

On August 17, 1972, plaintiffs Carlson and Yazzolino filed their class action complaint, for the reason that they were not included in the two sub-classes outlined by Judge Goodwin. The only difference between Williams and Carlson-Yazzolino is that Carlson-Yazzolino represent two additional sub-classes.

The Honorable Gus J. Solomon, District Court Judge, revoked the Williams classes on January 30, 1973, and disallowed the Carlson-Yazzolino classes. In doing so, Judge Solomon did not review or alter any of the findings made by Judge Goodwin.

Petitioners state that Williams admitted in his deposition that he did not rely upon and was not in-

[1] Appendix, pp. A-1, A-2.

fluenced by the prospectus in connection with his purchase. This is patently untrue. In their argument before Judge Solomon, defendants made this assertion, and Judge Solomon apparently made a good faith finding of such a fact, since it appears in his order. But, it is contrary to the record, since Williams most certainly read the prospectus; in his deposition, he states so time and again. In fact, he spent 30 minutes reading it. He was so impressed by it, he felt the company was doing him a favor in allowing him to buy more stock.

Petitioners refer to the fact finding of Judge Solomon, in his order of January 30, 1973, to the effect that defendant directors and officers admitted at the annual shareholders' meeting of October 20, 1969, that certain purchase orders for data processing equipment were not "firm" orders. In doing so, petitioners imply that the record that went to the Circuit Court of Appeals dealt only with the minor impropriety of an admission to stockholders, that the April prospectus was inaccurate in its claim of "firm" purchase back orders. Such is a seriously deficient impression. In fact, the "Statement of the Case" should have included some mention of the voluminous record that was forwarded to the Circuit Court of Appeals. This record included minutes of directors' meetings, depositions taken of defendant directors, and sworn affidavits. This record tends to support, without contradiction, many other factual matters, other than those mentioned in Judge Solomon's opinions, that were considered by the Cir-

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cuit Court of Appeals. A few bear mentioning: Defendants published in April, 1969, an enthusiastic $3 million prospectus, the third in a two year period, promising a mobile data processing product ready to market, boasting of over $1 million in back orders, when, in fact, the company was still experimenting and never ever produced a product, and, in fact, had no legitimate orders whatsoever. Forged "orders" and the bold assertion of a proven product that directors knew, and, when deposed, admitted was nothing more than an "idea," were only the two gawdiest of a steady stream of misleading information made to the public. Nevertheless, after having discovered that there were no back orders at all, the directors first held a directors' meeting and cautioned each other about the danger of telling shareholders the truth about the company, and then appeared at the annual shareholders' meeting in October, 1969, gave equivocal answers to direct questions on these subjects from shareholders, and failed to alert shareholders to the fact that (1) there were no back orders at all, "firm" or otherwise, and (2) there was, in fact, no product for sale.

Petitioners state that defendants paid certain monies into Court as a compromise to plaintiffs' claim. Petitioners fail to mention that no provision was made to inform the class of the proposed settlement, by the Court, though requested by plaintiffs, and mandated by Rule 23(e).

There was no compromise settlement. In fact, the amount paid into Court by defendants did not include

plaintiff's costs, or any provision for attorney fees, and ignored plaintiffs' claim for punitive damages.

I. The Circuit Court Affirmed Judge Goodwin's Findings in Granting Class Designation

The Honorable Alfred T. Goodwin, Circuit Court Judge, sitting as a District Court Judge by designation, made specific findings of class designation.[2] His order established the law of the case, and his decision should not be overturned by another judge later, in the absence of a showing of some change in the law of the case and a material reason for doing so. *Kempe* v. *U.S.*, 160 F.2d 406 (C.C.A. Iowa, 1947) cert. den. 331 U.S. 843; *GAF Corp.* v. *Circle Floor Co.*, 329 F. Supp. 823 (D.C. N.Y. 1971) affirmed at 463 F.2d 752 (2d Cir.); *Robb* v. *Sales*, 54 F.R.D. 196 (D.C. Pa. 1972).

No change had occurred in the law of the case on January 30, 1973, when Judge Solomon, acting sua sponte, reversed Judge Goodwin's prior order and revoked the class action designation in *Williams*.

II. The Ninth Circuit Reviewed the Entire Record on Reliance and Causation

The Ninth Circuit was not confined to a review of one item of evidence, i.e., the Williams deposition. Though plaintiff claims that a reading of the deposition points to reliance, and defendants claim the opposite, the Ninth Circuit could ignore this contentious area altogether. The Ninth Circuit had before it, for

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[2] Appendix, p. A-1.

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review, not the sufficiency of the evidence after a trial on the merits of the case, but the sufficiency of the allegations of plaintiffs' complaint for purposes of class designation.

Plaintiffs have alleged a common course of conduct consisting of the dissemination of a stream of false and misleading information, coupled with nondisclosure of the falsity thereof, over a period of time from 1967 through 1971. This deception, directed against all class members alike, was accomplished by standardized, printed material: prospectuses, press releases and reports to stockholders.

The Ninth Circuit agreed with Judge Goodwin that plaintiffs' complaint, together with the record on appeal, made the case ideally suited for class designation. A potential disagreement, at the time of trial, over the interpretation of one item of evidence, the Williams deposition, doesn't change the present broader decision of whether a class is or is not the better way to proceed.

III. Class Action Plaintiffs Cannot Ignore Their Fiduciary Duties to the Class.

Defendants have the right to confess judgment and pay into Court the amount of plaintiffs' claims. But plaintiffs are not obliged to draw down the monies deposited (1) when no provision is made to inform class members pursuant to Rule 23(e) and (2) when the amounts are disputed.

The Ninth Circuit had little choice but to reverse

on this issue when it learned that, though requested by plaintiffs, no provision was made to notify the class which had been previously designated and notified by Judge Goodwin, that there had been no hearing regarding disputed costs, that there had been no hearing regarding attorney fees, and that one of plaintiffs' causes of action was being ignored.

CONCLUSION

The Ninth Circuit correctly decided that these cases are appropriate for class designation. Certiorari should be denied.

DATED May 24, 1976.

Respectfully submitted,

BEN T. GRAY
Attorney for Respondents
Charles E. Williams, Dan R. Carlson, Frank Yazzolino

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APPENDIX

1. Judge Goodwin's Order Designating Class Action, filed April 12, 1972.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

CHARLES E. WILLIAMS,

Plaintiff,

v.

JAMES N. SINCLAIR, et al,

Defendants.

Civil No. 71-577

ORDER DESIGNATING CLASS ACTION

Plaintiff's motion to maintain a class action was denied by this court on December 9, 1971. On March 1, 1972, plaintiff moved this court to reconsider its earlier order, and, upon reconsideration, the court finds, pursuant to Fed. R. Civ. P. 23(a), (b) (3), that the representative plaintiff will fairly and adequately represent the interests of the class, that questions of law or fact common to the members of the class predominate over questions affecting only individual members, and that a class action is superior to other available methods of adjudicating this controversy.

IT IS THEREFORE ORDERED that the above-entitled action proceed as a class action. The class shall be composed of those persons who owned securities of the Data Pacific Corporation as of March 17,

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1969, and who, on or before May 1, 1969, exercised the warrants issued by the Corporation to existing shareholders. The class shall also include those persons who owned Data Pacific securities on the date the April 1969 prospectus was released and who retained such securities until August 19, 1971, the date this action was filed, or who, prior to August 19, 1971, but after May 1, 1969, sold such securities at a financial loss.

IT IS FURTHER ORDERED that plaintiff send notice to all members of the class in a form of notice to be approved by the court, and that plaintiff bear the costs of such notice.

DATED this 12th day of April, 1972.

/s/ *Alfred T. Goodwin*
United States Circuit Judge
sitting as District Judge
by designation